L&B LANDandBUILDINGS

NOVEMBER 2021

Not All Real Estate is an Inflation Hedge

Not All Real Estate is an Inflation Hedge

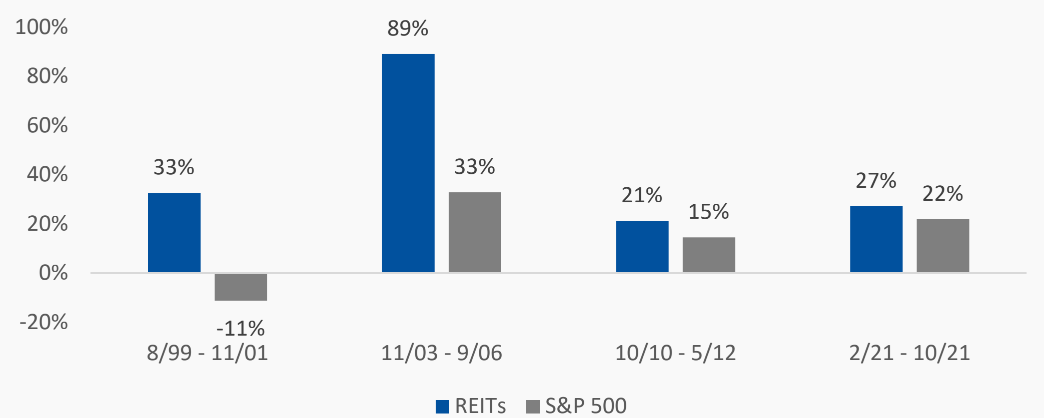
Last month the price consumers paid for goods and services increased by 6.2% compared to a year ago – the fastest 12-month pace in more than 30 years and the fifth straight month of inflation above 5%. Its impossible to ignore that we live in an increasingly inflationary world, and it's not clear whether that will be changing anytime soon. Logically, investors are looking for places of safety, as well as ways to capitalize on this environment.

Real estate offers investors protection, as rents are reset to higher market levels, replacement costs rise, and asset values increase. Real estate is an effective inflation hedge as the cost to build rises with inflation, limiting supply and forcing rents higher for well demanded properties to meet the demand. But not all real estate fits into the inflation hedge category. Investors must choose wisely. In our view, residential, self-storage and warehouses provide attractive inflation hedges, while office and net lease real estate are likely to be poor stores of wealth amid high inflation.

Real Estate Stocks Outperform as Inflation Accelerates

REIT stocks have historically posted outsized returns during periods of rising inflation. REITs have generated an average total return of 43% in the four periods of sustained rising core inflation since the modern REIT era began in 1994, outperforming the S&P 500 average return of 15%. This data set supports investor intuition that REITs are an effective inflation hedge.

REITS GENERATED OUTSIZED RETURNS WHEN INFLATION SEES SUSTAINED RISE



Source: Land & Buildings, Bloomberg

KEY POINTS

Public real estate can be an effective inflation hedge, but investors need to choose wisely

Real estate asset value and income growth have historically outpaced inflation

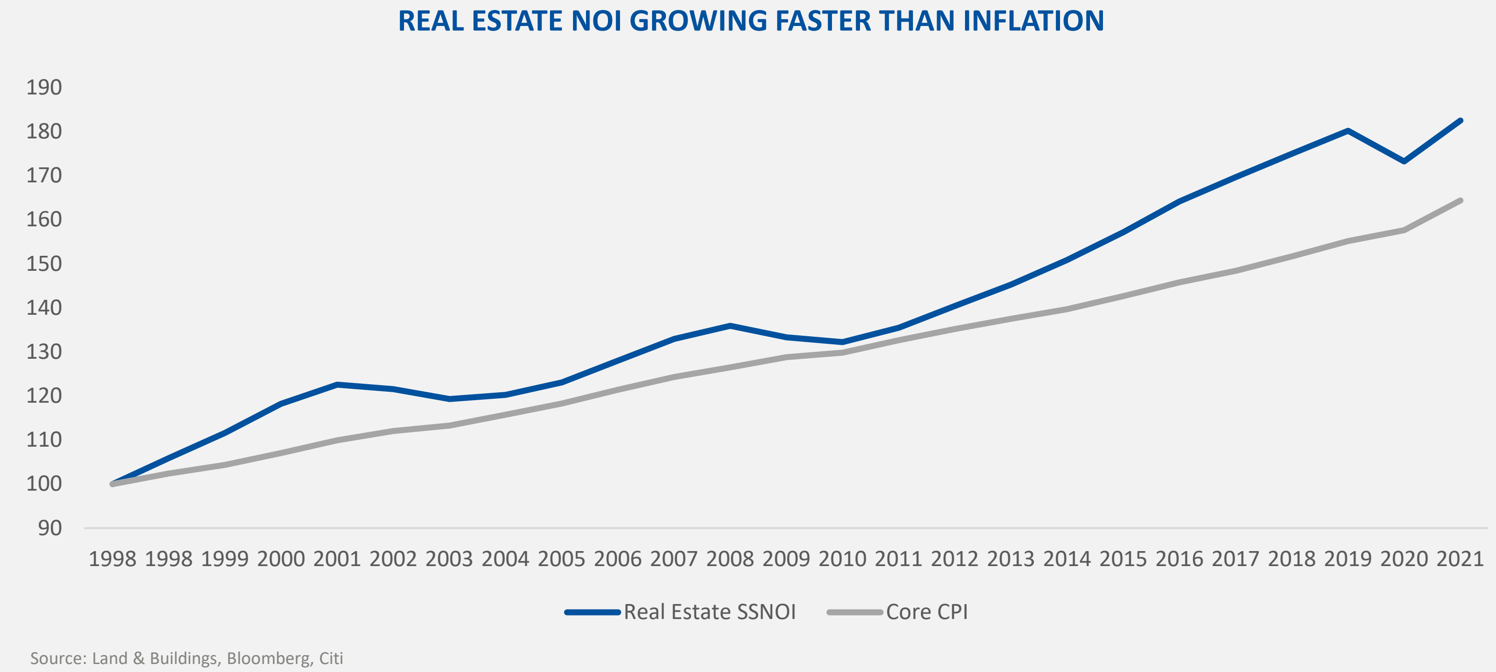
Residential, self-storage and warehouses provide the best inflation hedge today

Poor stores of wealth amid high inflation today include office and net lease

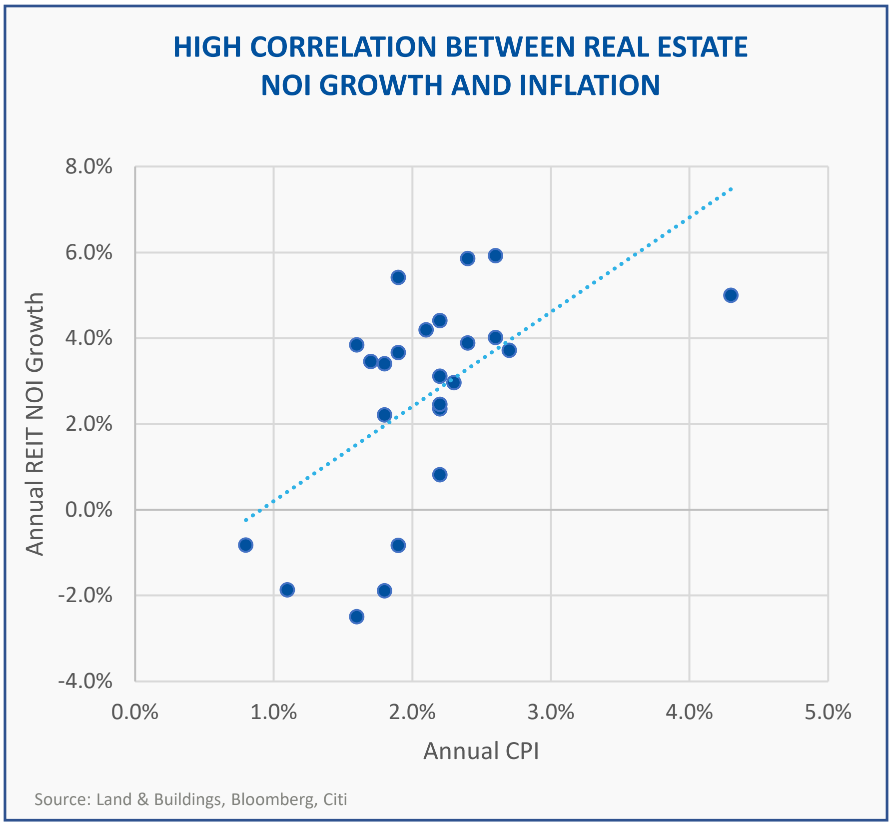
1 Landmark Square, 17th Floor, Stamford, CT 06901 • IR@landandbuildings.com
(203) 987-5827 • landandbuildings.com

Real Estate NOI Growth Has Materially Outpaced Inflation

Historically, real estate net operating income ("NOI") growth has also outpaced inflation, as measured by the Consumer Price Index (CPI). Cumulatively, REIT net operating income has grown 83% since 1998 versus a 64% compound rate of inflation.



Inflation has a clear and marked impact on the rate of net operating income growth at real estate companies, as evidenced in the exhibit on the right. Inflation and NOI growth have a 0.6 correlation since 1998, highlighting the tight relationship between real estate pricing power and core inflation. When inflation is particularly high, real estate NOI growth has been robust. Historically, when annual CPI has averaged more than 2.5%, REIT NOI growth was 4.7%. Economists expect another year of elevated inflation in 2022, with average expectations north of 3%, which positions real estate well for continued strong growth next year and beyond. REIT NOI is estimated to grow 8% in 2022.



Choose Your Inflation Protected Real Estate Carefully

Not all property is a potent inflation hedge, and it is imperative for investors to choose carefully. To protect against inflation, real estate needs pricing power. Shorter leases offer more immediate upside than long duration leases. Higher operating margins are superior to lower margin businesses, preserving income growth in the face of higher operating expenses. Low vacancy and tight supply are critical, as an oversupplied property sector will have difficulty raising rents until excess vacancy is absorbed. Real estate investments that meet the above criteria will be best positioned to win in a higher inflation environment.

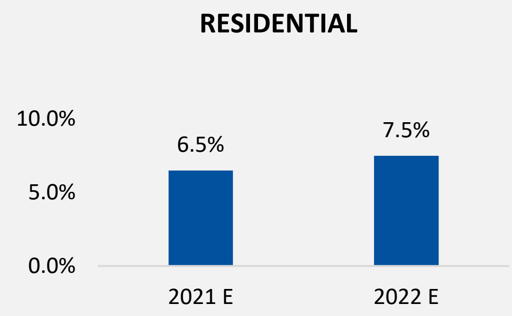
Seek an Inflation Hedge in Residential, Self-Storage and Warehouses

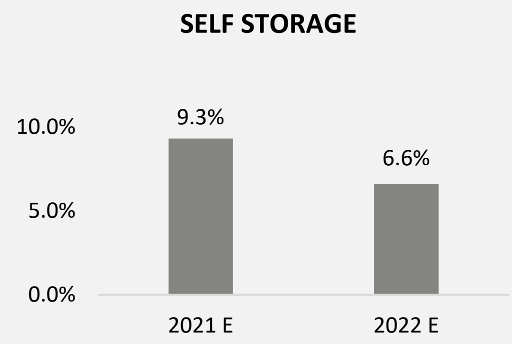
Residential assets, including multifamily and single-family rentals, are experiencing robust demand against a backdrop of a decade of underbuilding housing. National apartment and single-family rents are up more than 15% on average year-over-year. This spike in rents is real-time evidence of residential's inflation hedge characteristics. Leases are typically 12 months, and net operating income margins are high at ~70%, allowing for a quick repricing of rents and insulation from cost pressures. Supply chain disruptions and a difficult labor market for housing construction should further constrain supply. We believe AvalonBay (NYSE: AVB), a national apartment owner with a best-in-class development platform, and American Homes 4 Rent (NYSE: AMH), a single-family rental landlord with 50,000 homes, both own high quality residential real estate trading at a discount to net asset value (NAV) with attractive growth prospects.

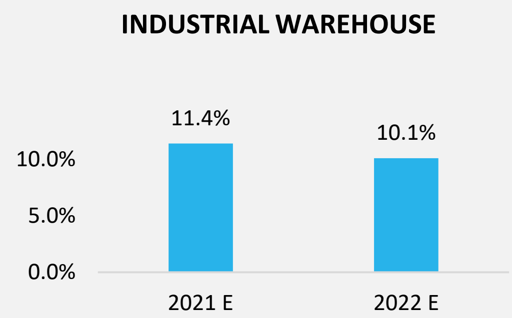
Similarly, self-storage is experiencing exceptional pricing power, with net effective rates up 40% from pre-COVID levels. The story again comes down to supply and demand. Storage is an underappreciated post-pandemic winner. The sector has new tailwinds that are likely to be long-lasting, including increased work from home (WFH) and robust housing activity. This strong demand is allowing landlords to fill up their storage facilities and push rents to record levels. The current supply environment is benign as new development completions are down 30% from their peak in 2019. This low level of new competition is expected to remain through at least 2022. With monthly leases, high margins and low operational intensity and capex, self-storage is likely to provide attractive inflation protection. Public Storage (NYSE: PSA), the largest self-storage landlord in the United States, should be well positioned to capitalize on these inflationary trends.

Industrial warehouse demand is surging. Secular and cyclical tailwinds and new construction levels are not keeping up with space needs. Industrial warehouse fundamentals were strong before the pandemic, and they have only strengthened. Accelerated adoption of e-commerce, higher inventory needs to avoid shortages, supply chain duplication and onshoring – along with stronger economic activity – are combining for record demand. New development starts are increasing but remain below demand. Mark to market on warehouse portfolios are in the 10 -25% range while rents are expected to rise another 5 - 10% in 2022. High margins and low capex needs again are critical components of preserving inflation protection. First Industrial (NYSE: FR) is an attractive value opportunity in the industrial warehouse sector, in our view.

STRONG RENTAL GROWTH EXPECTATIONS FOR APARTMENTS, SELF-STORAGE AND WAREHOUSES







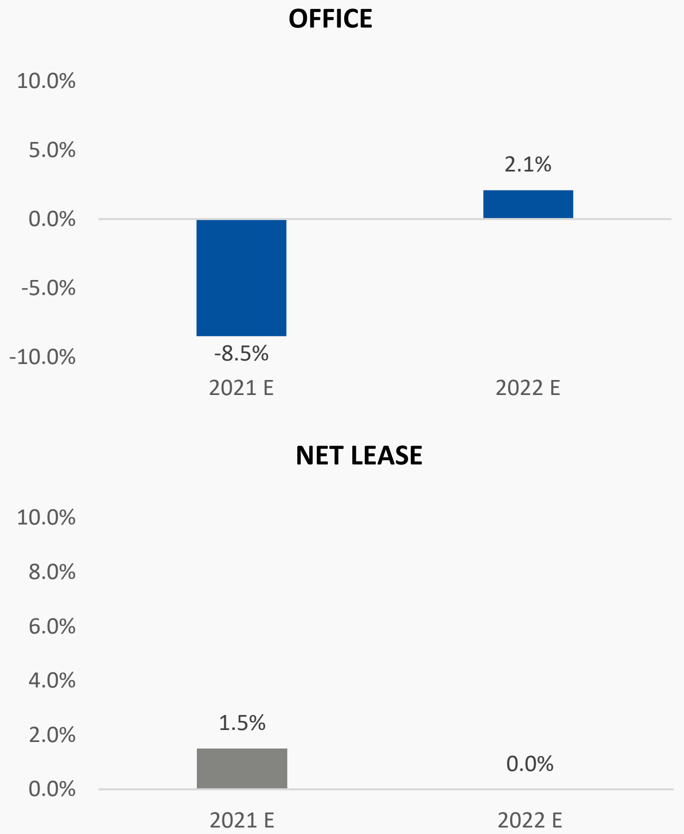
Poor Stores of Wealth Amid High Inflation — Office and Net Lease

Office real estate is unlikely to be a beneficiary of the current macroeconomic backdrop. As we highlighted in our May 2020 white paper (click here), office markets are facing an existential hurricane, particularly in gateway markets like New York City. Pre-COVID headwinds included high capex requirements, elevated new supply, and, in many coastal markets, unfriendly political and tax environments. Now the post-pandemic scramble of where people live and work has ushered in a new era of lower office utilization. Supply and demand dynamics are unfavorable, as incremental demand will go to filling up empty space as opposed to pushing rents. National vacancy rates are already breaching 2009 post-GFC levels at over 17%, according to Cushman & Wakefield. It is not clear occupancy losses have peaked yet in the US, as many large corporate office users are still in the process of determining their long-term office needs, with more looking to shrink footprints than expand. Additionally, office assets typically have low margins, particularly at below average occupancy levels. Layer in long-term leases that are likely to see rents reset lower upon expiration and elevated TIs (tenant improvement costs) to attract tenants and it's difficult to see how office is a relative winner with higher inflation.

Net lease REITs provide the most bond-like income streams to investors. The typical lease term is 10 - 15 years with modest annual rent escalators. Individual properties are usually fully leased by a single tenant and, in the public markets, focused on free-standing buildings operated by tenants such as pharmacies, restaurants, banks, gyms and movie theaters. The commodity-type space and limited annual lease expirations provide minimal near-term ability to pass inflationary rents on to tenants, resulting in these properties acting more like bonds, which decline in value as inflation accelerates. Net lease REITs have underperformed REITs when CPI has been greater than 2.5% as the lack of pricing power reduces attractiveness of the portfolios.

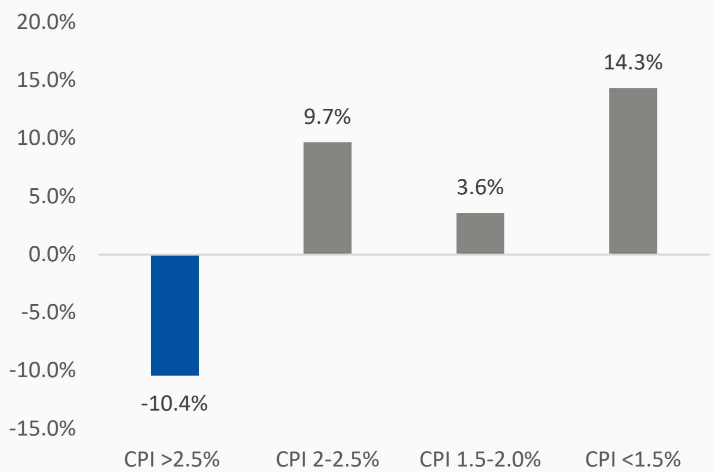
Publication Date: November 2021

LACKLUSTER RENTAL GROWTH FOR OFFICE AND NET LEASE



Source: Land and Buildings, Green Street; Note: Net Lease using same store NOI growth as a proxy to rental growth

NET LEASE ANNUAL TOTAL RETURNS UNDERPERFORM DURING HIGH INFLATION PERIODS



Source: Land and Buildings, Green Street, Bloomberg; Note: Data from 1998 to 2021 YTD, represents average annual out/under performance for each category

1 Landmark Square, 17th Floor, Stamford, CT 06901 • IR@landandbuildings.com
(203) 987-5827 • landandbuildings.com

Legal Disclosure

This White Paper is a summary for informational purposes only that does form the basis of any agreement. This White Paper is subject to a more complete description and does not contain all of the information necessary to make a decision with respect to an investment. Any offering of an investment may only be made to qualified investors pursuant to the relevant offering memorandum, containing material information concerning the relevant terms, fees, investment strategies and risks of an investment, and a definitive subscription agreement, both of which must be read in their entirety. No offer to purchase an investment will be made or accepted prior to receipt by an investor of such documents and the completion of all appropriate documentation. All investors must meet certain securities laws investor qualifications and other eligibility criteria, as described in the applicable offering materials, before they can make an investment.

Unless otherwise stated, opinions, calculations, and estimates included in this White Paper constitute the judgment of Land & Buildings and is subject to change without notice. The information in this White Paper is provided as of the date hereof and is believed to be accurate and/or derived from sources that Land & Buildings believes to be reliable; however, (i) such information has not been independently verified by any affiliated or previously affiliated institution and (ii) Land & Buildings does not make any representation or warranties, express or implied, regarding, or assume any responsibility for, the truth, accuracy, reliability, or completeness of any information contained in this White Paper.

Certain statements contained in this White Paper constitute "forward-looking statements" and such statements do not, nor are they intended to, constitute a promise of actual results. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual events or results or the actual performance of Land & Buildings to differ materially from those reflected or contemplated in this White Paper. No reWhite Paper or warranty is made as to future performance.

Any information in this White Paper is provided for informational purposes only and should not be deemed as a recommendation with respect to an investment. Accordingly, no prospective investor should make any investment decision on the basis of the information contained in this White Paper. Any liability on account of any party's use of or reliance on the information contained in this White Paper with respect to any such investment decision is hereby expressly disclaimed. Furthermore, this disclosure does not purport to be a complete itemization or explanation of the risks or considerations involved in an investment, nor is this White Paper intended to constitute legal, tax or accounting advice or investment recommendations. Prospective investors are strongly urged to obtain professional guidance from their tax, financial and legal advisers in evaluating all of the tax, financial and legal implications and risks involved in participating in an investment. An investment as discussed herein, like any investment, includes the risk of total loss.

In making an investment decision, investors must rely on their own examination of the information provided and the terms of any subsequent offering. No recommendation with respect to an investment has been made by any federal or state securities commission or regulatory authority, nor have the foregoing authorities confirmed the accuracy or determined the adequacy of this White Paper. Any representation to the contrary is a criminal offense.